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In the Supreme Court of the United States

OCTOBER TERM, 1954

CORN PRODUCTS REFINING COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

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In the Supreme Court of the United States

OCTOBER TERM, 1954

No. 457

CORN PRODUCTS REFINING COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

OPINIONS BELOW

The pertinent opinions of the Tax Court are (1) an opinion relating to the taxable year 1940 (R. 22–30; Pet. 25–33), reported at 16 T. C. 395, and (2) an unreported memorandum opinion (R. 201–215; Pet. 33–48) relating to the taxable year 1942.[1] The opinion of the Court of Appeals (Pet. 48–56) is reported at 215 F. 2d 513.

[1] In the 1942 case, the Tax Court subsequently rendered a supplemental opinion (R. 216–219), reported at 20 T. C. 503, with respect to a matter not pertinent to the present petition.

JURISDICTION

The judgment of the Court of Appeals was entered on August 25, 1954. (Pet. 48.) A petition for a rehearing (Record, following p. 291) was denied on September 27, 1954 (Pet. 2). The petition for a writ of certiorari was filed on November 22, 1954. The jurisdiction of this Court is invoked under 28 U. S. C., Sec. 1254.

QUESTIONS PRESENTED

1. Whether the Court of Appeals was correct in affirming the holding of the Tax Court that purchases and sales by taxpayer of corn futures on commodity exchanges were consummated in order to obtain protection for its manufacturing business and were comparable to hedges, and hence that such transactions resulted in ordinary, rather than capital, gains and losses within the purview of the Internal Revenue Code of 1939.[2]

2. Whether the Court of Appeals correctly affirmed the Tax Court's holding that the losses sustained by the taxpayer on such transactions in corn futures were not subject to the wash sales provision of Section 118 of the Code.

3. Whether, upon the facts, the Court of Appeals correctly affirmed the decision of the Tax Court that certain dividends declared by foreign corporations and payable to the taxpayer in its

[2] All Code references herein will be to the Internal Revenue Code of 1939.

base period year 1939, in currencies of Brazil and Italy, respectively, were so blocked by applicable foreign exchange restrictions as to not be includible in income for 1939 in arriving at the taxpayer's base period income for the purpose of computing its excess profits tax credit.

4. Whether the Court of Appeals was correct in deciding that Section 732 (c) of the Code deprived that court of jurisdiction to review the decision of the Tax Court with respect to whether certain income should be eliminated from the year 1941 as abnormal income within Section 721 of the Code for the purpose of computing the unused excess profits credit carryover from 1941 to 1942.

STATUTE INVOLVED

Sections 22, 41, 42, 112, 117, 118, 710, 711, 712, 713, 721, 729, and 732 of the Internal Revenue Code of 1939, the pertinent statutory provisions, are set forth in the Appendix, *infra*, pp. 19–31.

STATEMENT

The facts, as found by the Tax Court in the two cases before it (R. 22–25, 202–210) and as stated by the court below in its opinion (Pet. 48–56), may be summarized as follows:

Taxpayer is engaged in the manufacture and sale of corn products, including starches, sugar, sirups, oils, and feeds. The principal product obtained by the taxpayer from raw corn is starch.

Cerelose, one of its major products, is a refined sugar derived from starch which competes with cane and beet sugar. (R. 202.) Its plants have a daily grind capacity of 170,000 bushels, and a raw corn storage capacity of some 2,300,000 bushels, somewhat less than a three-weeks' supply. Between the years 1938 and 1942, its purchases of raw corn ranged from some 35,000,000 to some 60,000,000 bushels annually. (R. 202–203.)

Taxpayer's sales policy has been in general, with certain exceptions, to contract for shipment of its products within 30 days at specified prices, but to give the customer the benefit of market price if lower at the time of delivery. Its policy was also to cancel any unfilled portion of an order at a customer's request. (R. 203.)

For a number of years, it was taxpayer's practice to purchase and sell corn futures contracts through members of a commodity exchange.[3] Taxpayer engaged in futures transactions "as a part of its corn buying program", buying futures when the price was advantageously low, beginning

[3] The Tax Court found that a corn future is a contract calling for the delivery at a stated time, within 11 months or less, of 5,000 bushels of corn or some multiple thereof, of a stated quality, at a stated price. (R. 204.) A seller has the option of delivering the corn on any day during the month in which the contract matures, and of furnishing a different grade, with an appropriate price adjustment. The buyer furnishes his broker with "margin", or a percentage of the price, until delivery is taken or the contract is sold, at which time settlement is made.

its buying each year at harvest time, and selling most of its futures in the early summer if it then appeared that there would be no corn shortage and no great danger of higher prices. If the latter occurred, taxpayer gradually sold its futures as it bought for grinding. (R. 204.)

The futures were not included in taxpayer's inventory, its profits or losses on futures being shown in a "Corn Miscellaneous" account, and the net gain or loss for each year was debited or credited to cost of sales, being treated as a reduction of or addition to cost of goods sold. (R. 204.) For 1940, taxpayer had a net profit of some $680,000 from purchases and sales of futures (R. 24), and for 1942 it had a net loss therefrom of some $109,000. (R. 206.)

Taxpayer's purchases of corn futures did not constitute speculative transactions for profit, but were consummated in order to obtain business protection and to insure the profitable conduct of its business. (R. 206.)

In December of 1938, a Brazilian corporation (Maizena), wholly owned by taxpayer, declared a dividend payable in January of 1939, and set up on its books an account payable to taxpayer of 2,175,000 Brazilian milreis. There were foreign exchange restrictions in Brazil in 1939, restricting (to an extent not disclosed by the record) the transmission of funds out of that country. In 1939, taxpayer did receive out of its dividend

the amount of $4,862.31, the equivalent of 100,649.9 milreis, by bank draft, under circumstances not shown by the record. Taxpayer received the balance of that dividend in 1940. (R. 206–207.)

In 1939, dividends were also declared by certain Italian corporations of which taxpayer was a major stockholder, and the amounts payable to taxpayer, aggregating 4,496,327 lire, were credited by the corporations as accounts payable to taxpayer. There were exchange restrictions in force in Italy in 1939, restricting (to an extent not disclosed by the record) the transmission of funds out of that country. In the latter part of 1939, taxpayer converted the sums of 210,000 and 200,000 lire into United States dollars, through foreign exchange dealers in New York, at unofficial rates (approximately $0.021 per lira). (R. 207–209.)

Taxpayer's bookkeeping practice with respect to foreign dividends payable in blocked currency has been to set up the dividends as receivables, treating them as deferred income, and then recording the amount as income in the year of actual receipt in the United States. Its tax reporting practice has followed that bookkeeping practice. (R. 209.)

The dividends in controversy were not unqualifiedly subject to taxpayer's demand in the year 1939. In that year there was no market for the unconverted Brazilian milreis and the Italian lire

here in controversy, and no one could form an opinion as to their values in that year. (R. 209.)

Taxpayer had no excess profits tax liability for 1941, and in so determining, the Commissioner excluded from taxpayer's excess profits net income for that year the sum of $436,945.36 as abnormal income under Section 721 of the Internal Revenue Code. The Commissioner's computation of the taxpayer's unused excess profits tax credit carryover from 1941 to 1942 did not exclude from the taxpayer's excess profits net income for 1941 that amount of $436,945.36. (R. 210.)

The Tax Court, on the foregoing findings, held, contrary to taxpayer's contentions, (1) that taxpayer's gains and losses from its futures transactions are to be treated for tax purposes as resulting in ordinary income and losses and not as capital gains and losses; (2) that taxpayer's futures transactions are not within the wash sales provisions of Section 118 of the Code; (3) that taxpayer failed to establish its right to the adjustments it sought, so as to increase its 1939 income by the blocked foreign dividends in question, for the purpose of increasing its excess profits credit; and (4) that the amount of certain income was not to be eliminated from the year 1941 as abnormal income under Section 721 of the Code, for the purpose of determining taxpayer's unused excess profits carryover from 1941 to 1942, since

taxpayer had no excess profits tax liability for the year 1941. (R. 26–29, 211–214, 215.)

The Court of Appeals affirmed the Tax Court with respect to its first three holdings, but declined to review the fourth holding on the ground that because of the provisions of Section 732 (c) of the Code it lacked jurisdiction to review. (Pet. 48–56.) Hence, it dismissed the petition to review pro tanto.

ARGUMENT

1. The court below was clearly correct in holding that the resulting gains and losses from taxpayer's purchases and sales of futures are to be treated as ordinary income and losses under Code Section 22 (*infra*, p. 19), rather than as capital gains and losses under Code Section 117 (*infra*, p. 21). The Tax Court had found that taxpayer's purchases of futures did not constitute speculative transactions, but were availed of in order "to obtain business protection and to insure the profitable conduct of the business" (R. 206), and that while not conforming to the technical definition of hedging, taxpayer's transactions were "an integral part" of its manufacturing business, and therefore comparable to hedges. That holding is consistent with the rule, followed in the tax field for many years, that gains or losses from "hedging" transactions are properly considered as ordinary income and losses, and not as capital gains and losses. See G. C. M. 17322, XV–2 Cum. Bull. 151

(1936). *Grote* v. *Commissioner*, 41 B. T. A. 247; *Battelle* v. *Commissioner*, 47 B. T. A. 117; *Stewart Silk Corp.* v. *Comissioner*, 9 T. C. 174. See also *Commissioner* v. *Farmers & G. C. Oil Co.*, 120 F. 2d 772 (C. A. 5th), certiorari denied, 314 U. S. 683; *Trenton Cotton Oil Co.* v. *Commissioner*, 147 F. 2d 33, 35 (C. A. 6th), rehearing denied, 148 F. 2d 208. Cf. *Tennessee Egg Co.* v. *Commissioner*, 47 B. T. A. 558; *Commissioner* v. *Covington*, 120 F. 2d 768 (C. A. 5th), certiorari denied, 315 U. S. 822; *Estate of Makransky* v. *Commissioner*, 5 T. C. 397, affirmed per curiam, 154 F. 2d 59 (C. A. 3d).

The relation of a taxpayer's transactions in futures to his business is plainly a matter of a factual nature, and the affirmance by the Court of Appeals of the Tax Court's holding on this question is no more than a concurrence in the Tax Court's findings. It is settled that these concurrent findings, which are amply supported by the record, will not be reviewed here in the absence of exceptional error. *Comstock* v. *Group of Investors*, 335 U. S. 211, 214.

There is no merit to taxpayer's contention (Pet. 7–10) that the decision of the court below, insofar as it held that taxpayer's transactions in corn futures gave rise to ordinary income and losses, is in conflict with the cases of *Makransky* v. *Commissioner*, 154 F. 2d 59 (C. A. 3d); *Commissioner* v. *Farmers & G. C. Oil Co.*, 120 F. 2d

772 (C. A. 5th), certiorari denied, 314 U. S. 683, and *Trenton Cotton Oil Co.* v. *Commissioner*, 147 F. 2d 33, 35 (C. A. 6th), rehearing denied, 148 F. 2d 208.

As the opinion below indicates (Pet. 51–53), "hedging" is not a term of art defined in the tax laws. Despite apparent differences in terminology, the pertinent decisions of the lower courts are reconcilable in terms of their own facts and present no basic divergence with respect to the legal principles deemed controlling. Thus, in the *Makransky* case, there was involved only an isolated instance of dealings in futures, and not, as here, the consistent practice of a manufacturer availing itself of regular and continuous dealings in futures "for the purpose of stabilizing inventory cost" (Pet. 52). The Tax Court found there that the taxpayers had not used a method of hedging against present sales of its finished products and that their losses on futures transactions were therefore capital losses. The Third Circuit declined, by reason of this Court's decision in *Dobson* v. *Commissioner*, 320 U. S. 489, to review that finding of the Tax Court. In the *Farmers & G. C. Oil Co.* case, the taxpayer had no future commitments on hand to be protected from price variations. In the *Trenton Cotton Oil Co.* case, the taxpayer, a manufacturer of crude oil (for which there was no commodity market) engaged in dealings in futures of refined oil. Further-

more, at the time the taxpayer entered into its futures transactions in refined oil, it had already completed its sales of crude oil. Hence, its future dealings, unlike the instant case, were for the purpose of recouping losses already sustained.

In the instant case, the futures transactions "were entered into to stabilize inventory costs and thus protect profit" (Pet. 53), and the fact that taxpayer achieved only partial protection, *i. e.*, protection only against increases in the price of corn, was not significant, since, as the court below held, whether the futures transactions were utilized to obtain "complete or only partial insurance" was "simply a difference in degree, not in kind" (Pet. 53).[4]

2. On the second question, the court below, in affirming the Tax Court, held that the wash sales provisions of Section 118 of the Code, *infra*, p. 21, were not applicable to taxpayer's transactions in corn futures, because commodity futures cannot be regarded as "securities" within the meaning of that Section and because a new futures commodity contract is not "substantially identical" with any prior futures contract within the meaning of Section 118. We believe that the decision of the court below is correct. The very

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[4] In the court below, petitioner contended that the courts had set up a "judge-made exception" from capital gains or losses treatment as to hedging in commodity futures (Pet. 51). It may be noted that Section 1233 of the Internal Revenue Code of 1954 expressly incorporates such exception.

nature of corn futures would seem to preclude a holding that they are "securities" within the purview of Section 118. And there are indications that Congress did not intend the term "securities" in Section 118 to have so broad a meaning as to include corn futures. Cf. Sections 23 (g) (3) and (k) (3) and 373 (f), and also Section 112 (b) (1) with Sections 332 (b) and 502 (c) of the Internal Revenue Code. It will be observed that in the latter two provisions Congress expressly referred to transactions in commodity futures.

It is true, nevertheless, as taxpayer asserts, that there is a direct and express conflict on this question (see Pet. 53) between the decision of the court below in the instant case and the decision of the Sixth Circuit in the case of *Trenton Cotton Oil Co.* v. *Commissioner*, 147 F. 2d 33. In view of that conflict, we do not oppose the granting of the writ of certiorari to review the second question presented in the petition for a writ of certiorari (Pet. 2). However, the importance of the question appears to be circumscribed. The precise problem does not appear to be one of frequent occurrence,[5] and the 1950 amendment to Section

[5] After the decision in the *Trenton Cotton Oil Co.* case in 1945, the problem does not appear to have again recurred in litigation until the instant case, notwithstanding the fact that the *Trenton Cotton Oil Co.* decision was directly contrary to the rationale of the decisions in *Harriss* v. *Commissioner*, 143 F. 2d 279 (C. A. 2d), and *Valley Waste Mills*

117 of the Code may greatly restrict application of the question to future cases.[6]

3. The Tax Court held that certain Brazilian and Italian dividends were not includible in taxpayer's income for 1939, because they were blocked by foreign exchange restrictions. In so holding, the Tax Court concluded that taxpayer had failed to meet the burden resting upon it of establishing that the foreign dividends were freely convertible into United States dollars in 1939. The affirmance of this holding by the court below was correct and consistent with settled procedural principles.

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v. *Page*, 115 F. 2d 466 (C. A. 5th), certiorari denied, 312 U. S. 681, to which the court below referred in expressing its inability to agree with *Trenton Cotton Oil Co.*

Moreover, the real significance of the applicability of Section 118 in this case lies in the fact that there is involved the determination of the base period income (for the years 1936 through 1939) under the so-called Second World War Excess Profits Tax Law, in which connection taxpayer would, by the application of Section 118, be permitted to eliminate wash losses aggregating $3,100,000 for the years 1938 and 1939 alone. See R. 230.

[6] The plain effect of Section 117 (l), which was added to the Internal Revenue Code of 1939 by Section 211 of the Revenue Act of 1950, c. 994, 64 Stat. 906, would be to limit materially the scope within which the second question is pertinent with respect to dealings in commodity futures. See H. Rep. No. 2319, 81st Cong., 2d sess., pp. 94–96 (1950–2 Cum. Bull. 380, 448–449; S. Rep. No. 2375, 81st Cong., 2d sess., pp. 44–45 (1950–2 Cum. Bull. 483, 515–516). See also R. 29; and Mim. 6243 (1948–1 Cum. Bull. 44), as amended by Mim. 6789 (1952–1 Cum. Bull. 38). Cf. Sec. 1233 of the 1954 Internal Revenue Code.

The decision of the court below on this question to the effect that the "evidence amply supports the Tax Court's conclusion that the petitioner failed to prove free convertibility" (Pet. 55), turned upon the facts and circumstances of this particular case. Taxpayer, however, endeavors to carve out of this issue a refined legal problem as to "the burden of going forward" with the evidence, and asserts that in that respect the decision of the court below is in conflict with *Whitney* v. *Commissioner*, 73 F. 2d 589 (C. A. 3d). (Pet. 12–13.) The contention is without substance.

Taxpayer offered proof merely that in 1939 it converted (at rates considerably below current foreign exchange rates) approximately 100,000 milreis and 410,000 lire into dollars. There was no showing of the manner of conversion. Manifestly, this proof was insufficient to make out a prima facie case that the blocked dividends aggregating 2,175,000 milreis and 4,496,000 lire were freely convertible into United States dollars during the year 1939. Hence, the problem whether the Commissioner was legally charged with the burden of going forward with the evidence did not arise. In the circumstances, it is plain that there is no conflict between the case of *Whitney* v. *Commissioner*, *supra*, and the decision of the court below.

4. The court below properly declined, because of the prohibition contained in Section 732 (c) of the Code, *infra*, pp. 30–31, to review the decision of the Tax Court on the question involving abnormal income under Section 721 of the Code, *infra*, pp. 27–29.

On this question, the decision below is clearly in accord with several decisions in which appellate courts have observed the prohibition of Section 732 (c) against review of "abnormalities" questions under the excess profits tax law of the Second World War, namely: As to a question under Section 721 (*James F. Waters, Inc.* v. *Commissioner*, 160 F. 2d 596 (C. A. 9th), certiorari denied, 332 U. S. 767), as to a question of Section 711 (b) (1) (J) and (K) (*Colonial Amusement Co. of Philadelphia* v. *Commissioner*, 173 F. 2d 568 (C. A. 3d); *Colorado Milling & El. Co.* v. *Commissioner*, 205 F. 2d 551 (C. A. 10th)), or a question under Section 722 (*George Kemp Real Estate Co.* v. *Commissioner*, 182 F. 2d 847 (C. A. 2d), certiorari denied, 340 U. S. 852).

There is no conflict, as alleged (Pet. 13), with *Stimson Mill Co.* v. *Commissioner*, 163 F. 2d 269 (C. A. 9th), certiorari denied, 332 U. S. 824, rehearing denied, 332 U. S. 839; *Dowd-Feder, Inc.* v. *Commissioner*, 173 F. 2d 673 (C. A. 6th); or *Packer Pub. Co.* v. *Commissioner*, 211 F. 2d 612 (C. A. 8th). In the *Stimson Mill* and *Dowd-Feder* cases, decisions of the Tax Court were held

to be reviewable because viewed as involving questions turning on sections *other* than the "abnormalities" sections specified in Section 732 (c). See *George Kemp Real Estate Co.* v. *Commissioner, supra,* p. 849. In the *Packer Pub. Co.* case, the Court of Appeals merely remanded the case to the Tax Court for consideration of an issue as to the right to relief under Section 711 which the Court of Appeals concluded had been (improperly) not passed upon by the Tax Court.[7]

Contrary to the taxpayer's assertion (Pet. 14), the issue which the court below declined to review was one which had arisen and had been determined "solely by reason of" Section 721. See R. 202, 215, and *San Francisco Stevedoring Co.* v. *Commissioner,* 8 T. C. 222, 226–228. Specifically, the issue was whether, in determining the taxpayer's excess profits tax for 1942, certain income could be eliminated from the year 1941 as abnormal within Section 721 for the purpose of computing an unused excess profits credit carryover from 1941 to 1942 even though there was no excess profits tax liability at all, or in

[7] It may be noted that the statements made by the Eighth Circuit in the *Packer Pub.* case (p. 616) as to the scope of the prohibition of Section 732 (c) and as to the holding of the Second Circuit in the *Kemp* case constitute nothing more than dicta.

any event, in 1941. In disposing of the issue, the Tax Court followed its holding in the *San Francisco Stevedoring* case, where it had rejected a similar contention on the ground that it was not supported by the statute (8 T. C., p. 227).

The Tax Court's decision on this issue is correct. As indicated by the Tax Court in the *San Francisco Stevedoring* case (p. 227), the simple but conclusive answer to the contention is that, since the purpose of Section 721 is to give relief so that the excess profits tax for a particular taxable year shall not exceed the tax as provided in Section 721, and since the taxpayer had no excess profits tax liability at all for 1941, Section 721 could have no application to that year. In short, that Section cannot be properly applied merely to increase the excess profits credit carry-over of a year for which no excess profits tax is due.

CONCLUSION

The decision of the court below on Questions Nos. 1, 3, and 4, stated in the petition for certiorari, is clearly correct, there is no conflict of decisions on those issues, and further review thereof is not warranted. The petition should be denied as to those questions. In view of the conflict of decisions on Question No. 2, we do not oppose the granting of the writ to review that question; however, as indicated, *supra*, pp. 12–13,

this Court may consider that the question lacks sufficient general importance to warrant resolution of the conflict at this time.

Respectfully submitted,

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DECEMBER 1954.

APPENDIX

Internal Revenue Code of 1939:

CHAPTER 1—INCOME TAX

* * * * *

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

(26 U. S. C. 1946 ed., Sec. 22.)

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *

(26 U. S. C. 1946 ed., Sec. 41.)

SEC. 42. PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED.

(a) *General Rule.* The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under section 41, any such amounts are to be properly accounted for as of a different period. * * *

(26 U. S. C. 1946 ed., Sec. 42.)

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

* * * * *

(26 U. S. C. 1946 ed., Sec. 112.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *Definitions.*—As used in this chapter—

(1) *Capital Assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l). * * *

* * * * * *

(d) *Limitation on Capital Losses.*—

(1) *Corporations.*—In the case of a cor-

poration, losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. * * * *

* * * * *

(26 U. S. C. 1946 ed., Sec. 117.)

SEC. 118. LOSS FROM WASH SALES OF STOCK OR SECURITIES

(a) In the case of any loss claimed to have been sustained from any sale or other disposition of shares of stock or securities where it appears that, within a period beginning 30 days before the date of such sale or disposition and ending 30 days after such date, the taxpayer has acquired (by purchase or by an exchange upon which the entire amount of gain or loss was recognized by law), or has entered into a contract or option so to acquire, substantially identical stock or securities, then no deduction for the loss shall be allowed under section 23 (e) (2); nor shall such deduction be allowed under section 23 (f) unless the claim is made by a corporation, a dealer in stocks or securities, and with respect to a transaction made in the ordinary course of its business.

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(26 U. S. C. 1946 ed., Sec. 118.)

CHAPTER 2—ADDITIONAL INCOME TAXES

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[8] As applicable to the year 1942, after amendments by Section 212 (a) of the Revenue Act of 1939, c. 247, 53 Stat. 862, and Section 150 (c) of the Revenue Act of 1942, c. 619, 56 Stat. 798, this provision was as follows:

(d) *Limitation on Capital Losses.*—

(1) *Corporations.*—In the case of a corporation, losses from sales or exchanges of capital assets shall be allowed only to the extent of gains from such sales or exchanges.

SUBCHAPTER E—EXCESS PROFITS TAX

[As added by Section 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974, which provided that the new subchapter may be cited as the "Excess Profits Tax Act of 1940"].

SEC. 710. IMPOSITION OF TAX.

(a) [as amended by Section 201 (a) of the Revenue Act of 1941, c. 412, 55 Stat. 687, and Section 202 of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Imposition.*—

(1) *General Rule.*—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess-profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

* * * * *

(b) [as amended by Section 2 (a) of the Excess Profits Tax Amendments of 1941, c. 10, 55 Stat. 17, and by Section 204 (a) of the Revenue Act of 1942, *supra*] *Definition of Adjusted Excess Profits Net Income.*—As used in this section, the term "adjusted excess profits net income" in the case of any taxable year means the excess profits net income (as defined in Section 711) minus the sum of:

(1) *Specific exemption.*—A specific exemption of $5,000;

(2) *Excess profits credit.*—The amount of the excess profits credit allowed under Section 712; and

(3) *Unused excess profits credit.*—The amount of the unused excess profits credit adjustment for the taxable year, computed in accordance with subsection (c).

(c) [as amended by Section 204 (b) of the Revenue Act of 1942, *supra*] *Unused Excess Profits Credit Adjustment.*—

(1) *Computation of Unused Excess Profits Credit Adjustment.*—The unused excess profits credit adjustment for any taxable year shall be the aggregate of the unused excess profits credit carry-overs and unused excess profits credit carry-backs to such taxable year.

(2) *Definition of Unused Excess Profits Credit.*—The term "unused excess profits credit" means the excess, if any, of the excess profits credit for any taxable year beginning after December 31, 1939, over the excess profits net income for such taxable year, computed on the basis of the excess profits credit applicable to such taxable year. For such purpose the excess profits credit and the excess profits net income for any taxable year beginning in 1940 shall be computed under the law applicable to taxable years beginning in 1941. The unused excess profits credit for a taxable year of less than twelve months shall be an amount which is such part of the unused excess profits credit determined under the first sentence of this paragraph as the number of days in the taxable year is of the number of days in the twelve months ending with the close of the taxable year.

(3) *Amount of Unused Excess Profits Credit Carry-Back and Carry-Over.*—

(A) *Unused Excess Profits Credit Carry-Back.*—If for any taxable year beginning after December 31, 1941, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-back for each of the two preceding taxable years,

except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such unused excess profits credit over the adjusted excess profits net income for the second preceding taxable year computed for such taxable year (i) by determining the unused excess profits credit adjustment without regard to such unused excess profits credit, and (ii) without the deduction of the specific exemption provided in subsection (b) (1).

(B) *Unused Excess Profits Credit Carry-Over.*—If for any taxable year beginning after December 31, 1939, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-over for each of the two succeeding taxable years, except that the carry-over in the case of the second succeeding taxable year shall be the excess, if any, of the amount of such unused excess profits credit over the adjusted excess profits net income for the intervening taxable year computed for such intervening taxable year (i) by determining the unused excess profits credit adjustment without regard to such unused excess profits credit or to any unused excess profits credit carry-back, and (ii) without the deduction of the specific exemption provided in subsection (b) (1). For the purposes of the preceding sentence, the unused excess profits credit for any taxable year beginning after December 31, 1941, shall first be reduced by the sum of the adjusted excess profits net income for each of the two preceding taxable years (computed for each such preceding taxable year (i) by determining the unused excess profits credit adjustment

without regard to such unused excess profits credit or to the unused excess profits credit for the succeeding taxable year, and (ii) without the deduction of the specific exemption provided in subsection (b) (1)).

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(26 U. S. C. 1946 ed., Sec. 710.)

SEC. 711. EXCESS PROFITS NET INCOME.

(a) *Taxable Years Beginning After December 31, 1939.*—The excess profits net income for any taxable year beginning after December 31, 1939, shall be the normal-tax net income, as defined in section 13 (a) (2), for such year except that the following adjustments shall be made:

(1) *Excess profits credit computed under income credit.*—If the excess profits credit is computed under section 713, the adjustments shall be as follows:

* * * * *

(B) [as amended by Section 207 (a) of the Revenue Act of 1942, *supra*] *Gains and Losses From Sales or Exchanges of Capital Assets.*—There shall be excluded gains and losses from sales or exchanges of capital assets held for more than 6 months.

* * * * *

(2) *Excess profits credit computed under invested capital credit.*—If the excess profits credit is computed under section 714, the adjustments shall be as follows:

* * * * *

(26 U. S. C. 1946 ed., Sec. 711.)

SEC. 712 [as amended by Section 13 of the Excess Profits Tax Amendments of 1941, *supra*]. EXCESS PROFITS CREDIT—ALLOWANCE.

(a) *Domestic Corporations.*—In the case of a domestic corporation which was in ex-

income before January 1, 1940, the excess profits credit for any taxable year shall be an amount computed under section 713 or section 714, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. * * *

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(26 U. S. C. 1946 ed., Sec. 712.)

SEC. 713 [as amended by Section 4 of the Excess Profits Tax Amendments of 1941, *supra*, and Section 228 (c) (2) of the Revenue Act of 1942, *supra*]. EXCESS PROFITS CREDIT—BASED ON INCOME:

(a) *Amount of Excess Profits Credit.*—The excess profits credit for any taxable year, computed under this section shall be—

(1) *Domestic Corporations.*—In the case of a domestic corporation—

(A) 95 per centum of the average base period net income, * * *

* * * * *

(b) *Base Period.*—

(1) *Definition.*—As used in this section the term "base period"—

(A) If the corporation was in existence during the whole of the forty-eight months preceding the beginning of its first taxable year under this subchapter, means the period commencing with the beginning of its first taxable year beginning after December 31, 1935, and ending with the close of its last taxable year beginning before January 1, 1940; * * *

* * * * *

(26 U. S. C. 1946 ed., Sec. 713.)

SEC. 721 [as amended by Section 5 of the Excess Profits Tax Amendments of 1941, *supra*, and Section 221 (a) of the Revenue Act of 1942, *supra*]. ABNORMALITIES IN INCOME IN TAXABLE PERIOD.

(a) *Definitions.*—For the purposes of this section—

(1) *Abnormal income.*—The term "abnormal income" means income of any class includible in the gross income of the taxpayer for any taxable year under this subchapter if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of 125 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence.

(2) *Separate classes of income.*—* * *

* * * * *

(3) *Net abnormal income.*—The term "net abnormal income" means the amount of the abnormal income less, under regulations prescribed by the Commissioner with the approval of the Secretary, (A) 125 per centum of the average amount of the gross income of the same class determined under paragraph (1), and (B) an amount which bears the same ratio to the amount of any direct costs or expenses, deductible in determining the normal-tax net income of the taxable year, through the expenditure of which such abnormal income was in whole or in part derived as the excess of the

amount of such abnormal income over 125 per centum of such average amount bears to the amount of such abnormal income.

(b) *Amount Attributable to Other Years.*—The amount of the net abnormal income that is attributable to any previous or future taxable year or years shall be determined under regulations prescribed by the Commissioner with the approval of the Secretary. In the case of amounts otherwise attributable to future taxable years, if the taxpayer either transfers substantially all its properties or distributes any property in complete liquidation, then there shall be attributable to the first taxable year in which such transfer or distribution occurs (or if such year is previous to the taxable year in which the abnormal income is includible in gross income, to such latter taxable year) all amounts so attributable to future taxable years not included in the gross income of a previous taxable year.

(c) *Computation of Tax for Current Taxable Year.*—The tax under this subchapter for the taxable year, in which the whole of such abnormal income would without regard to this section be includible, shall not exceed the sum of:

(1) The tax under this subchapter for such taxable year computed without the inclusion in gross income of the portion of the net abnormal income which is attributable to any other taxable year, and

(2) The aggregate of the increase in the tax under this subchapter for the taxable year (computed under paragraph (1)) and for each previous taxable year which would have resulted if, for each previous taxable year to which any portion of such net abnormal income is attributable, an amount

equal to such portion had been included in the gross income for such previous taxable year.

(d) *Computation of Tax for Future Taxable Year.*— * * *

* * * * * *

(e) *Application of Section.*—This section shall be applied only for the purpose of computing the tax under this subchapter as provided in subsections (c) and (d), and shall have no effect upon the computation of base period net income. For the purposes of subsections (c) and (d)—

(1) Net abnormal income means the aggregate of the net abnormal income of all classes for one taxable year.

(2) Under regulations prescribed by the Commissioner with the approval of the Secretary, the tax under this subchapter for previous taxable years shall be computed as if the portions of net abnormal income for each previous taxable year for which the tax was computed under this section were included in the gross income for the other previous taxable years to which such portions were attributable.

(3) If both subsections (c) and (d) are applicable to any current taxable year, subsection (d) shall be applied without regard to subsection (c), and subsection (c) shall be applied as if the tax under this subchapter, except for subsection (c), was the tax computed under subsection (d) and as if the gross income and the other amounts necessary to determine the adjusted excess profits net income were those amounts which would result in the tax computed under subsection (d).

(f) *Abnormal Income From Exploration, Etc.*— * * *

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(26 U. S. C. 1946 ed., Sec. 721.)

SEC. 729. LAWS APPLICABLE.

(a) *General Rule.*—All provisions of law (including penalties) applicable in respect of the taxes imposed by Chapter 1, shall, insofar as not inconsistent with this subchapter, be applicable in respect of the tax imposed by this subchapter.

* * * * *

(26 U. S. C. 1946 ed., Sec. 729.)

SEC. 732 [as added by Section 9 of Excess Profits Tax Amendments of 1941, *supra,* and as amended by Sections 222 (c) of the Revenue Act of 1942, *supra,* by Section 2 of the Joint Resolution of June 30, 1945, c. 211, 59 Stat. 295, and by Section 203 (a) of the Act of December 29, 1945, c. 652, 59 Stat. 669]. REVIEW OF ABNORMALITIES BY THE TAX COURT OF THE UNITED STATES.

(a) *Petition to Tax Court.*—If a claim for refund of tax under this subchapter for any taxable year is disallowed in whole or in part by the Commissioner, and the disallowance relates to the application of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, relating to abnormalities, the Commissioner shall send notice of such disallowance to the taxpayer by registered mail. Within ninety days after such notice is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the ninetieth day) the taxpayer may file a petition with the Tax Court for a redetermination of the tax under this subchapter. If such petition is so filed, such notice of disallowance shall be deemed to be a notice of deficiency

for all purposes relating to the assessment and collection of taxes or the refund or credit of overpayments.

(b) *Deficiency Found by the Tax Court in Case of Claim.*—If the Tax Court finds that there is no overpayment of tax in respect of any taxable year in respect of which the Commissioner has disallowed, in whole or in part, a claim for refund described in subsection (a) and the Tax Court further finds that there is a deficiency for such year, the Tax Court shall have jurisdiction to determine the amount of such deficiency and such amount shall, when the decision of the Tax Court becomes final, be assessed and shall be paid upon notice and demand from the collector.

(c) *Finality of Determination.*—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Tax Court.

(d) *Review by Special Division of the Tax Court.*—The determinations and redeterminations by any division of the Tax Court involving any question arising under section 721 (a) (2) (C) or section 722 with respect to any taxable year shall be reviewed by a special division of the Tax Court which shall be constituted by the presiding judge and consist of not less than three judges of the Tax Court. The decisions of such special division shall not be reviewable by the Tax Court, and shall be deemed decisions of the Tax Court.

(26 U. S. C. 1946 ed., Sec. 732.)

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